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# THE WOMAN

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## *In This Issue*

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J U N E 1 9 4 8

*Official Publication*

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AMERICAN SOCIETY OF WOMEN ACCOUNTANTS

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## EDITORIAL

### ANNUAL MEETING

Plans for the joint annual meeting of AWSCPA and ASWA in Chicago on September 17, 18 and 19 are in progress. Details will be announced later—but please note the dates. The convention of the American Institute of Accountants is also being held in Chicago beginning September 20 and we hope that many of our members will take advantage of the opportunity to attend both in one trip.

### BERCU CASE

The decision on the Bercu case, in which the New York County Lawyers Association sought unsuccessfully to enjoin Bernard Bercu, a New York CPA, from rendering certain tax services on the ground that they constituted illegal practice of law, has been reversed by the Appellate Division of the Supreme Court.

The New York State Society of CPA's has announced that it will appeal.

### WOMEN AND JOBS

*Collier's* is authority for the statement that in the past five years women have been employed in all but three of the 451 occupations listed by the U. S. Census Bureau. The three positions are those of fireman in municipal fire departments and engineer and fireman on railroad locomotives.

*The News* reports that the Prudential Insurance Company of America, which during the war hired hundreds of married women to work in its offices, has made the policy a permanent one for peacetime. Company officials announced that hiring of married women will be continued and that the company will permit women to retain their jobs after marriage. Of 42,000 current employees, about 12,800 are women.

Miss Helen Maud Cam, distinguished authority on English constitutional history and lecturer on history at Cambridge University, England, is the first woman appointed to a full professorship on the Harvard University faculty. Beginning in the

fall Miss Cam will give courses in medieval history for Radcliffe and Harvard students.

At New York University a tradition was broken when the first woman was initiated into honorary membership in Perstare et Praestare, non-athletic honor society. She is Alice Dembska, secretary to the director of student activities, who frequently has taken over the duties of the director.

### REGIONAL CONFERENCES

Two highly successful joint AWSCPA/ASWA regional conferences were held in May.

The first marked the tenth birthday of ASWA and was held in its natal city, Indianapolis, on May 15 and 16. In attendance and in the caliber of the entertainment provided it was an outstanding event. Mrs. Hope Bedford Nevitt spoke at the Saturday evening banquet on the Bogota revolution with an eloquence that made the evening an unforgettable experience for her listeners. A social program followed the banquet and on Sunday a luncheon followed the business sessions. All events were held at the Indianapolis Athletic Club. To Indianapolis chapter go our congratulations and our thanks.

The West Coast joint regional conference was held on May 22 and 23 at the Claremont Hotel, Berkeley, California. Detailed reports on the happenings have not been received as we go to press but the program included a luncheon on Saturday, at which Marion Frye, first vice-president of ASWA and second vice-president of AWSCPA, spoke, and a banquet on Saturday evening at which the scheduled speaker was Perry Mason, Dean of the School of Business Administration at the Berkeley Campus of the University of California. Sunday featured breakfast on the beautiful and world-famous Lido Deck. The West Coast conferences have always been delightful occasions, and have whetted our appetite for the 1948 convention to be held in Los Angeles.

# TAX NEWS

TENNIE C. LEONARD, C.P.A., *Memphis, Tennessee*

Of paramount interest in tax circles since the last packet of Tax News was written has been the passage of the Revenue Act of 1948 which became a part of our revenue laws on April 2nd, effective retroactively, so far as income taxes are concerned, to January 1, 1948. The fact that it grants the first substantial reduction in many years to individual taxpayers and will result in millions of erstwhile taxpayers in the lowest bracket being relieved of the necessity for filing any income tax returns, has been widely publicized.

Personal exemptions and credits for dependents have been increased to \$600; and individuals 65 and over get an additional exemption of \$600. The allowance for the blind has been upped to \$600 and changed from a deduction to the more advantageous status of an exemption. The maximum optional standard deduction has been raised from \$500 to \$1,000 for single persons. The maximum total optional standard deduction will also be \$1,000 for married couples.

The reduction of 12.6% in tax rates on incomes up to \$2,000; of slightly more than 7.4% on incomes ranging from \$2,000 to \$137,719.10, and of approximately 5% on larger incomes, has generally been considered cause for rejoicing, even though tax and budget experts generally predict that the reduction will be short lived. Governmental fiscal experts have warned that it may be necessary to restore taxes, even above the 1946-47 rates, for the calendar year 1949.

While the reduction in individual tax rates is beneficial to all individual taxpayers, greater benefits will be derived by taxpayers in the middle and upper brackets from the "income splitting" provisions of the new law—the greater the disparity between the incomes of the husband and wife in the higher brackets, the greater the benefits. This has placed taxpayers in non-community property states on a basis equal to that of the residents of community property states and has removed a gross inequity from our tax laws. We think Stanley Surrey, formerly legislative counsel of the Treasury Department, who first advocated this move and whose "Surrey Plan" has been followed in the greater part in the new law, should receive proper recognition from the relieved taxpayers.

Much less widely advertised than the income tax reductions are the changes made by the 1948 Act to estate and gift tax provisions of the Code. Of the two, the estate and gift revisions may prove to be the more advantageous to taxpayers with large estates.

Prior to 1942, it was held that only one-half of the joint estate owned by married couples in community property states was taxable in the estate of the decedent, either husband or wife, and the remainder was the property of the surviving spouse. In 1942 Congress amended the estate tax law, the practical effect being that even in community property states all of the community property was includible in the husband's estate, if he predeceased the wife; or one-half of the estate was taxed in the wife's estate if she died first, with proper allowance, of course, for property acquired by either from non-community funds or from compensation for personal services.

The 1948 Act not only restores the benefits of community property rights taken away by the 1942 laws, but grants the same advantages to taxpayers in non-community property states, and extends it to gift taxes. This is accomplished by what is called the "marital deduction," which is allowed where any part of the deceased person's estate passes, or has passed, to the surviving spouse. The property so passing is deductible in computing the net taxable estate to the extent that it is includible in the gross estate, with the limitation that the marital deduction may not exceed 50% of the adjusted gross estate. The estate tax changes apply to estates of decedents dying after December 31, 1947.

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For gift tax purposes, the community property status is effected by using the "gift splitting" provisions where the gift is from both husband and wife to a third party, and the marital deduction where the gift is from one spouse to another.

While newspapers generally, tax commentators to a lesser degree, and even trust officers have apparently overlooked the drastic reduction in future estate tax levies, one group has not failed to grasp its significance and is now endeavoring to turn it to the utmost advantage of their clients and themselves. We refer to our friends, the ever present life insurance salesmen, who were not slow to see that their fields had suddenly expanded.

Long handicapped by the elimination in 1942 of the deduction from the gross estate of life insurance owned by the decedent and payable to named beneficiaries, life insurance underwriters sometimes found it difficult to convince their clients of the advantages of purchasing life insurance for the purpose of providing funds for the payment of the eventual estate tax, when such funds would also add to the burden of estate taxes to be met.

With the new 1948 Revenue Act making it possible, in effect, to reduce the taxable estate by one-half, and at the same time increasing the specific exemption, for practical purposes, from \$60,000 to \$120,000, estates previously subject to estate taxes will be exempt entirely in many instances. Those estates previously taxed at such rates that insurance was an expensive asset of the estate, may now be planned in such a way as to be taxed at rates so much lower than formerly that such estates can well pay the price for the liquidity afforded by life insurance.

At the same time, the increase in gift tax exemptions, resulting from application of the marital deduction and gift splitting, will enable many taxpayers to make substantial gifts without the payment of gift taxes. Later the donee, if a member of the family, may be convinced of the soundness of investing the money in insurance on the life of the donor—the suggestion, of course, should come from the insurance salesman, not from the donor.

Our life insurance friends are probably well aware, too, of the importance, at least to them, of one of the recommendations of the Staff of the Joint Committee on Internal Revenue Taxation. This Committee, which is assisting the House Ways and Means Committee in the preparation of the General Tax Revision Bill, expected to become law

later during the present session of Congress, has proposed the elimination of the "payment of premiums" test introduced into the Internal Revenue Code by the 1942 law. This new section, which has been approved by the Ways and Means Committee, will provide that the taxability of the proceeds of life insurance policies, payable to specific beneficiaries, will be determined exclusively by whether or not the decedent possessed incidents of ownership in the policy at the time of his death, with due regard, of course, to the contemplation of death feature in the case of policies assigned. Such a change, in conjunction with the increased specific exemption on gifts from husband to wife, will enable taxpayers to make gifts in greater amounts and suggest or specify that such gifts be used for the purchase of insurance on the life of the donor.

\* \* \*

The 1948 Revenue Act with its "income splitting" feature has rendered useless schemes for dividing income between husband and wife, but taxpayers (or tax practitioners) will continue to devise plans for reducing income taxes still further by dividing income with other members of the family. Consequently, the cases dealing with the division of income are still of interest.

In a recent case an inventor owned several patents on automobile repair machinery. The inventor-taxpayer gave a corporation, of which he was president and an 89% stockholder, non-exclusive contracts under which the corporation could manufacture and sell the patented machine subject to a royalty of 10% of the gross sales price. Taxpayer gave some of his contracts with his corporation to his wife.

The Tax Court held that the gift of the contract did not shift the royalty income from these contracts to the wife; the Circuit Court said that it did. The Supreme Court agreed with the Tax court and found that taxpayer had retained too many strings to his property. As an 89% stockholder of the licensee, taxpayer could have cancelled the contract when he desired, or could have regulated the royalties payable, since the contracts did not provide for a minimum royalty and did not require the manufacture of any particular number of machines. In addition, taxpayer remained the owner of the patents and could have licensed others, since the agreement was non-exclusive.

In its decision, the Supreme Court brushed aside the issue of whether the con-

(Continued on page 13)

# COAST - TO - COAST

MARGUERITE GIBB, C.P.A.

Seattle, Washington

MARGUERITE REIMERS, C.P.A.

## CHICAGO

A joint meeting in March with the Business and Professional Women's Club, at which members of the Export Managers Club and the Foreign Division of the Chicago association of Commerce and Industry were present, heard a discussion of America's foreign policy as well as a review of what is happening abroad. In April Lowell C. Doak, Director of Instruction in Higher Accountancy at LaSalle University, spoke of auditing standards in the light of releases from the American Institute of Accountants.

## CLEVELAND

The March issue of *The Figurehead*, monthly bulletin of the Cleveland Chapter, announced a forum, scheduled for May, on how to prepare for the CPA examinations. The chapter has a representative, Gertrude Hunkin, on the Inter-Club Council of Greater Cleveland, and her comprehensive report was a feature of this issue.

## DETROIT

Members of Phi Gamma Nu, national sorority in commerce, were guests of the chapter in March when Gloria Dunbarger spoke on "Back to the Buyer's Market." Mrs. Dunbarger, a partner in an advertising agency specializing in industrial, manufacturing and food products, is a speaker much in demand in the Detroit area.

Jennie Palen, in the city on an audit, was a most welcome guest at the February meeting.

## GRAND RAPIDS

The education dinner proved to be a huge success; the many teachers and students who attended were eager to hear of the chapter's vocational council project and the merit award. Other meetings featured Walter Bass, of the sales department of Radio Station WOOD, who spoke on "Human Relations in Living" and Arthur Neil, Jr. of the Michigan Bell Telephone Co. on "Pipelines."

Presentation of an honorary membership to Julia Norse, first president and sponsor of the chapter, was made by Lenore Harder and Ida Vanderweise at Julia's home in Tallahassee, Florida.

## INDIANAPOLIS

Speaking on "Repairs and Replacements" at the March meeting, K. B. Parrish, CPA, commented that while the line between repairs and replacements is somewhat finely drawn, a replacement seems to be anything the Internal Revenue Bureau won't let you use for repairs.

## LOS ANGELES

Lois Williamson, junior accounting student at UCLA, received the chapter's \$100 scholarship award at the March meeting, as well as a paid-up membership in the chapter through the next fiscal year.

B. A. Buchfield, chief investigator, Division of Corporations, State of California, described Los Angeles as the bunko center of the world. Mr. Burchfield described promoters' deals, their methods and manners, and said that women investors are not more gullible than men.

Forty members were guests of the National Cash Register Company at a buffet supper and demonstration of machine accounting.

## NEW YORK

At a joint meeting with Phi Chi Theta, Charles A. Corbin, CPA, senior partner of Frank E. Dixon and Company, spoke on "Changes in the Accounting Profession Over a Quarter of a Century," and on the same program Frank J. Scott, president of the Bankers Security Life Insurance Company, spoke on "Banking and its Relation to Present-Day Economy." Virginia Wood, president of the Atlanta chapter, was a welcome guest on this occasion.

J. Arthur Marvin, past president of the New York State Society of CPA's, spoke on "Progress of the Profession" at the May meeting.

## SAN FRANCISCO

A preview of an article "How Did We Get This Way" to appear later in *THE WOMAN C.P.A.*, based on questionnaires completed by chapter members, was presented by Dr. Catherine Quire and her public relations committee. "Current Trends in Balance Sheet and Report Terminology" was the subject of a talk delivered by Clifford V. Heimbucher.

San Francisco was most happy to welcome to a meeting Mary Gildea and Harriette Challenger of the Chicago chapter and on another occasion Ella Harrod of New York.

### SEATTLE

Eleven women accounting majors from the University of Washington were guests of the chapter at the April meeting when John Day, attorney, discussed "Shall I Incorporate My Business."

Ida Ezra, second vice president of ASWA, reviewed the changes made by current tax legislation on federal income tax payments in this state.

### TOLEDO

Paul Brooks, insurance executive, speaking in January, and Roy G. Bowersock, tax consultant, speaking at the February meeting, both decried the recent court reversals of many "timehonored" decisions.

### SUCCESSFUL CANDIDATES

Congratulations to the following, who passed the November 1947 CPA examinations:

Michigan: Jane Starr, 1700 Dime Building, Detroit 26.

Colorado: Barbara Ann Whirry, 495 Downing Street, Denver.

Ohio: Dorothy M. Coulter, 5704 Summit Street, Sylvania; Ednah Hewitt Jurey, 6000 Harvard Ave., Cleveland 5.

Utah: Delia E. McDermott, 2222 Eye Street, N. W., Washington, D. C.

### NEW AWSCPA MEMBERS

AWSCPA welcomes as new members: Mary Ellen Brickner, 930 First National Bank Bldg., Denver; Dorothy M. Coulter, 5704 Summit St., Sylvania, Ohio, with Wideman, Madden, Dolan & Co., 1600 Toledo Trust Bldg., Toledo; Ruth Dorothea Hoerich, 2823 N. Whipple St., Chicago, with Barrow, Wade, Guthrie & Co., 1 N. LaSalle St., Chicago; Mary J. Kaltenbach, 3902 Juniper Rd., Baltimore 18, with Sherwood Bros., Inc., Baltimore Trust Bldg., Baltimore 3; Alice Peckham, 9 Capitol Street, Concord, N. H.; Freda Shapiro, with Loeb and Troper, 501 Fifth Ave., New York 17; Elizabeth Adams Sterling, 500 Grand Theatre Bldg., Atlanta; Mildred Teitz, 21 Jarvis Place, Trenton, N. J.; Altha Myrl Thompson, 25 Roanoke Avenue, N. E., Atlanta; Ruth Ellene Ware, 6612 Travis Street, Houston 5, with Baker, Botts, Andres & Parish.

### NEW ASWA MEMBERS

New members of ASWA are welcomed by the following chapters: CHICAGO, Anne Bogue and Edwina Baskin, a transfer from Seattle; DETROIT, Gwenn Woodrow, Estelle Goodman, Angela Lynch, and Mildred Hanes, Wanda Jaskula, Alowyn Natche, Jane Starr; SAN FRANCISCO, Genevieve M. Baskfield and Gwynne G. Kohler; SEATTLE, Marie Snekvich, Mildred Bartels, Muriel McGuire, Mary Hoyt, and Velva Ames; CLEVELAND, Thelma D. Hahn, Florentine A. Lubecky, Rose Helen McMann, Elsie A. Roth, Myrtle G. Schwab, Elva Ann Simon, Cleo Wilson Strohmeier, Beatrice E. Bechtel, Lois M. Boehmer, Elizabeth Brugh, Norma Chervenak, Evelyn W. Davis, Dorothy M. Dutton, Helen M. Frantz, Ruth Howard, Marion E. Latimer, Ada Mac Geary, Zorka Pavlov, Josephine Skodis, Eva Speir, Luise Stutz, and Eleanor M. Zahm.

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### RECIPIENT OF ASWA SCHOLARSHIP SPEAKS

Miss Jacqueline Brown, junior member of Grand Rapids chapter ASWA, who received the \$100 scholarship awarded by that chapter in 1947, spoke briefly before the Secretarial Club of Grand Rapids Junior College on April 7 on the subject of opportunities for women in accounting.

Miss Brown's interest in ASWA and her rapid progress in her studies are evidence, not only of her abilities, but of the constructive value of ASWA's scholarship project.

### THE PRESS

The March 1948 issue of *The Accountants Digest* contains reprints of the following articles from THE WOMAN C.P.A.:

Tax avoidance and Tax Evasion, by John J. Raymond

Women—Not Accountants—Who Have Served Accountancy, by Norman E. Webster

Preparation of large Quantities of Dividend Checks, by Phyllis M. Haan (The Idea Exchange)

English for the Accountant, by Jennie M. Palen

The May 1948 issue of *The Journal of Accountancy* contains a note of San Francisco ASWA chapter's \$100 scholarship given to the University of California for an award to a woman student in business administration.





*Earle H. Cunningham is president of The Institute of Internal Auditors, Inc. and a past president of its Detroit chapter. He is a graduate of Portland University with the degrees of B.S.C. and M.S.C. and had several years of public accounting and university teaching experience before joining General Motors Corporation as a traveling auditor in 1926. He served successively as supervising auditor and assistant general auditor before his appointment as general auditor of the corporation in 1943.*

*He is a certified public accountant of the States of Maine, Indiana and Ohio, a member of the American Institute of Accountants and of the American Accounting Association, and author of several articles on internal auditing and staff training.*

*This paper was the subject of a talk before the Detroit Chapter ASWA in February. We present, with pleasure and pride, an article packed with information which is valuable to both the public and the private accountant.*

## FUNCTIONS AND RESPONSIBILITIES OF THE INTERNAL AUDITOR

By **EARLE H. CUNNINGHAM, C.P.A., General Auditor**  
**General Motors Corporation**

Auditing is somewhat analogous to law in respect to the marketing of one's skill. As you know, some lawyers open up an office of their own, or join with others already in practice, and offer their services to the public. Other lawyers prefer to associate with private industry as legal advisors.

The person who has trained and specialized in auditing has a similar choice as to the field in which he or she will seek employment, i.e., enter the public accounting field or associate with private industry as an internal auditor.

Because the progress made by internal auditing during the past ten years has been greater than in any prior period, and is accelerating each year, I feel that there will be an increasing number of opportunities in this particular field as time goes on.

### NATURE OF INTERNAL AUDITING

Current concepts of internal auditing are quite different from those of a few years ago. Objectives, scope of duties and responsibilities have broadened materially. Management is becoming increasingly conscious of the utility of internal auditing and is making far greater use of it than it has in the past.

In the days of the sole proprietorship and

the small partnership, the owners took a very active part in the management of their business. Most activities stemmed from their directives and the main operating functions were under their direct control or supervision. There were, however, certain exposures that could not be controlled satisfactorily. The accounting and record keeping were largely hand operations performed by employees with little more than clerical qualifications; and the systems of internal control and internal check were of an elementary character. As a result errors were a common occurrence and misappropriations were comparatively easy.

This condition developed the need for someone with more than ordinary skill to follow along behind the constructive accounting to ferret out the many clerical errors and to detect any misappropriation of assets. This simple activity of policing company values and clerical routines was termed Internal Auditing.

In a way this was about all that was required, since the problems of management and administration were comparatively few, and proprietary management was in a position to exercise necessary controls. With the introduction and development of the corporate system, business enterprises grew in size and complexities to the point

"owner" administration was impossible or ineffective. The owners or proprietors could no longer exercise that direct and personal control that was possible in the small business unit operated as a sole proprietorship or small partnership.

With the growth of the corporate system came the introduction of accounting and office machines, improved and intricate accounting systems, perfected systems of internal check and the employment of more skillful employes. These developments caused radical changes in audit requirements and a demand for a higher standard of practice on the part of the auditor.

Today, the size of most companies makes it impossible for the executives composing top management to exercise direct and personal supervision of the functions for which they are responsible. About all they can do is to formulate policies and procedures, and review and interpret reports on operations. They can no longer observe and participate in the multiplicity of detail transactions that flow through the records at a dizzy pace.

While the executive has bridged this ever-widening gap between his administrative position and the front line operations by surrounding himself with a corps of assistants and line supervisors, he nevertheless is operating by remote control.

It matters not how able his staff may be, nor how well the integrated pattern of management may be formed, defects and deterioration are sure to develop unless vigilant surveys and evaluations are maintained.

Recognizing that inspection of management functions and clerical routines is as essential as inspection on the production line, management utilizes internal auditing for the purpose of assuring itself that policies and procedures are properly and faithfully followed, that company values are adequately protected and conserved, and to secure the benefit of an independent and objective review and appraisal of its accounting, operating routines and other responsibilities.

The older concepts of internal auditing emphasized its objectives as:

1. The detection and prevention of fraud.
2. The detection and prevention of error.

Current concepts not only recognize these same objectives, but include many others which are considered of far greater worth to management. The number of instances of deliberate dishonesty or undetected clerical errors are few in comparison with the

cases in which management acts on incomplete or inaccurate information; or the number of instances that the business suffers through waste, hazards, exposures, lack of internal check, ineffective controls, failure of delegated responsibilities and matters of this kind.

Present practice groups internal auditing objectives as follows:

1. Those which are essentially protective.
2. Those which are essentially constructive.

It is the rendering of those services that are classified as "essentially constructive" that has caused internal auditing to be recognized as a tool of management.

The internal auditor who renders no more than "protective" services has not yet attained professional status; he is merely performing a clerical routine—a policing service.

The problems of business administration are becoming more numerous and complex with each succeeding year, with the result that executives at all levels are finding it necessary to parcel out more and more of their responsibilities to subordinates for execution.

In our larger companies this increasing need for decentralization of authority and a corresponding realignment of responsibilities has resulted in layer upon layer of subordinate management. For illustration:

1. Top management—
  - (a) Proprietary management
  - (b) Administrative management
2. Middle management—
  - (a) Staff management
  - (b) Operating management
3. Line management—
  - (a) Department management
  - (b) Supervisory management

And to this grouping might be added other subdivisions, as section management, group management, field management, branch management, plant management and many others.

Each management layer receives its responsibilities from its superior level and directs and coordinates the activities of management segments to which it has delegated a portion of the responsibilities received.

## TOOLS OF MANAGEMENT

Experience has proved that efficiency and par of performance are seldom obtained from delegated responsibilities. The factors of misinterpretation, carelessness, incompetency, procrastination, misunder-

standing, neglect, poor judgment, and many other human weaknesses tend to defeat the desired objectives.

For this reason management has found it necessary to establish a system of internal controls which will assure that their policies, procedures and directives are faithfully and effectively carried out; that company values are adequately protected and conserved; that there has been a proper administration of functions delegated; that management information has been accurately accumulated and presented; that external regulations have been complied with; and that matters requiring consideration are promptly drawn to attention.

The number of individual controls making up such a system, will vary, naturally, with the type of business, size of the company, and the requirements of management. As an example we have:

1. Budgetary control
2. Cost control
3. Production control
4. Cash control
5. Internal check
6. Internal auditing
7. Many others of a similar nature .

Each type of control has its own important part to play in the general scheme of management; and the most of them interlock with the general pattern of operations to such an extent that they become an integral part of it.

While "internal auditing" is one of the several controls maintained to serve management, it differs from most of the other types of control, in that it forms no part of the action phase of business. It supplements rather than complements the other controls, and functions largely as a protective and service agency.

In addition to functioning as a type of control for measuring and evaluating the effectiveness of other controls, internal auditing serves management by keeping it posted on the state of business by bringing to attention all material facts that might not otherwise receive consideration.

As previously pointed out the objectives of internal auditing may be classified under two general headings; those which are:

1. Essentially protective
2. Essentially constructive

The protective objectives comprehend the policing of such features as the following:

1. Company policies
2. Accounting and operating procedures
3. Systems of internal check
4. Care and storage of records

5. Care and storage of company values
6. Compliance with external regulations
7. Reliability of accounting and statistical data
8. Many other analogous functions

While the auditor is charged with a rather wide and varied type of policing service, including the detection of fraud and error, it is the constructive services he renders that enhance the value of his work.

The utility of a tool depends upon a complete knowledge of what the tool will do and the skill that is applied to that tool. This analogy is equally true in respect to internal auditing. The utility of internal auditing depends upon a comprehensive knowledge of what it can do for management, and the degree of skill the auditor is able to apply. The worth of internal auditing and its utilization by management are in ratio to the auditor's knowledge and his skill in the application of that knowledge.

To function at the management level as opposed to the clerical level, the auditor must possess more than mere technical knowledge. Too many persons concentrate on becoming good technicians without learning how to use their skill effectively. They develop their specialized technical skill far beyond the broad knowledge they need to support that skill.

What the average auditor needs more than anything else is a broader knowledge of his company's affairs and a better understanding of its problems and objectives.

The auditor must have a clear and comprehensive understanding of the entire structure of controls and checks which management has established, if he is to perform an effective policing service.

He should be familiar with the by-laws of his corporation, the minutes of stockholders' and directors' meetings, the extent to which the directors have delegated responsibilities to management, the general duties of management executives and the extent to which any of these duties have been redelegated to subordinates, and many other matters of a similar nature.

He should also be provided with a copy of the company's organization chart that he may be thoroughly familiar with the relationship of the various functional activities and know who is responsible for their operation.

In those cases where staff and department operating manuals are available, the auditor should be furnished with a copy for each activity in order that he may be well informed on their routines and procedures.

Copies of all policy letters and instruc-

tions relating to operating routines and procedures that may be issued by executives and department heads should be supplied to the auditor that he may be kept currently informed of any matters which affect his policing and service activities.

The auditor should be invited to sit in on all meetings of committees, executives, department heads and other groups which in any way relate to policies, procedures, reorganizations and other activities, in order that he may be as familiar as possible with management's thinking and objectives. Otherwise how can he serve this group to the fullest measure?

He should also be promptly advised of all important contracts, royalty and license agreements, expansion and rearrangement projects, construction programs and similar activities, that he may be prepared to give them the required attention.

He should be thoroughly familiar with the policies, procedures, and functions of such departments as the following:

- a. Accounting
- b. Financial
- c. Purchasing
- d. Production
- e. Marketing
- f. Salvage
- g. Labor relations
- h. Public relations
- i. Other principal activities

The auditor should be a constant student of his company's business. The more he knows about its problems and objectives, the greater will be his worth. He should develop a management consciousness and perspective that will enable him readily to sense those matters that are of interest to those whom he serves.

It is only when internal auditing is established at the management level, headed by a highly capable director and staffed by competent personnel, that management can derive the maximum benefits from its service.

## ORGANIZATIONAL TYPES OF INTERNAL AUDITING

There are four "organizational" types of internal auditing, and a failure to recognize this fact is, perhaps, the principal reason for the lack of a common understanding that frequently exists when people are discussing internal auditing. The objectives, scope of audit, and required standard of practice differ materially with each type.

The four types are:

1. Proprietorship internal auditing
2. Management internal auditing
3. Staff internal auditing
4. Department internal auditing

When the internal auditor is appointed by, and reports to the owner of a sole proprietorship, the partners of a partnership, or the directors of a corporation (or the stockholders), and is completely independent of all other management personnel, he is termed a "proprietorship" internal auditor. His scope of activities is generally very broad and he is highly concerned with operating and management functions and their effectiveness.

If the internal auditor is appointed by the president, the executive vice president, the administrative or executive committee of a corporation, or other management authority of a similar level, and he is independent of all other personnel below these strata, he is termed a "management" internal auditor. Usually his duties and responsibilities will not differ materially from those of the "proprietorship" type. However, he is a representative of administrative management and not of proprietorship.

In those cases where the internal auditor is appointed by a vice president in charge of finance, the treasurer, the controller, or by some other staff head of relative rank, he is said to be a "staff" internal auditor. As such, he has no authority to function outside of the staff head's area of responsibility, except as his staff head may arrange with other staff managers. In addition the auditor is subject to the instructions, policies and dictates of his staff head. Generally he lacks the full independence and freedom of action enjoyed by a "proprietorship" or "management" auditor.

When a department of a staff or some other minor operating activity appoints an internal auditor to serve within the limits of that activity's responsibility, the auditor is termed a "department" internal auditor. Examples of this type would be:

1. Disbursement auditor
2. Payroll auditor
3. Accounts payable auditor
4. Construction auditor
5. Branch auditor
6. Others of a similar nature

In respect to this type of internal auditing one must carefully distinguish between those department activities that are truly of an auditing nature and those activities that are merely a part of the system of

internal check. We must make a clear distinction between "internal check" and "internal audit." "Internal check" is a control designed to function as an integral part of the accounting system while "internal audit" is a type of control created to function independently of accounting routines and procedures.

Internal auditing is a term that has been very loosely used, and has been applied to all types of verification work from simple clerical routines up the scale to the performance of complex assignments comparable to those of the public accountant. Consequently when we deal with this term we must be conscious of its wide connotations, and appreciate the need for clarification as to specific type.

In the absence of qualifications to the contrary, the term "internal auditing" is generally understood to refer to the "staff" or "management" type, and to comprehend both protective and constructive objectives.

#### FUNCTIONAL TYPES OF INTERNAL AUDITING

In considering internal auditing, we not only have to recognize its organizational level but also its functional type. The objectives, scope of work, audit technique, style of reporting, and other details of operations will vary considerably with each functional type of auditing. The more common types are as follows:

1. Continuous audits
2. Feature audits
3. Periodic audits

Continuous audits may be classified as:

- A. Pre-audits
- B. Post-audits

Continuous audits of the pre-audit type are generally employed when it is desired to have all transactions independently verified before finalization. This form of auditing is performed largely by "department" internal auditors, such as disbursement auditors, accounts payable auditors and payroll auditors.

Continuous audits of the post-audit type differ only in respect to time of performance; the audit is usually carried out at the auditor's convenience following consummation of the transaction but before transfer of the related records to closed files.

Feature auditing consists of examining one phase of the program at a time; such as cash receipts, payrolls, plant accounts, et cetera. The program is so arranged that all features will be covered at least once each year, and some will be serviced two

or more times depending upon requirements. This method is employed largely by resident internal auditors.

Contrasted to the feature auditing procedure just explained, the periodic audit covers all features for a definite period, at one time; this may be quarterly, semiannually, yearly, or at irregular intervals.

Period audits are generally applied when a company maintains operating and accounting activities at more than one location. Generally speaking, resident auditors perform feature audits while traveling auditors make periodic examinations.

When the "continuous" type of auditing is used, reports are usually rendered on a monthly basis; however, the frequency of reports should conform to management's requirements.

When the auditor is following a "feature" audit program, he should render his report upon completion of each major feature or group of related features. If his work schedule calls for periodic examinations, then his report should be submitted promptly upon completion of his assignment.

The type of auditing to be employed depends entirely upon organizational set-up and objectives to be accomplished. Internal audit systems do not come in stock patterns; they have to be specially designed to fit the needs of each particular type of business and management's requirements, if they are to be effective service agencies.

Whenever two or more people get together for a discussion of internal auditing, it is essential that they first define the organizational and functional types they have in mind in order that they may proceed from a common viewpoint.

#### SPECIAL QUALIFICATIONS FOR AUDITING

I believe it might be interesting and perhaps helpful to mention a few of the qualifications necessary to successful internal auditing.

A good fundamental education of high school grade, naturally, is a first requisite. While college training is not a necessity, it is of course a desirability. Broad training in business subjects is preferable to specialization, though one should major in accounting and auditing.

The subjects that are most important and highly necessary are those that many give little consideration, and this is not only true in respect to those training for auditing, but equally true in respect to those training for other professional activities.

The subjects that are so woefully neglected are—

1. Communications
2. Human relations

Ineffective communication is a universal weakness, but it stands out like the north star on a clear night, with those who have to express the product of their efforts by the medium of the pen. You will find auditors who can do an excellent job so far as performing an audit is concerned, but when their work is completed and they face the problem of rendering a formal report on their examination, they fall from the pinnacle of professionalism to the depths of an amateur. And I would like to emphasize that this weakness is not limited to auditors alone. The most striking defect in the average professional man is his inability to convey his thoughts, correctly, clearly, concisely, courteously, and with character to his composition. These are the five C's of report writing.

During the past year I have talked with many directors of auditing staffs and they all tell me that their biggest problem is to find auditors who can construct a satisfactory report.

While I feel it is, primarily, the individual's responsibility to qualify himself in this

important subject, I also feel that our schools and colleges have been extremely backward in developing effective courses in communication.

Human relations is another subject that few persons have mastered sufficiently to use it effectively. Superior contact ability is a quality that most executives seek in filling important positions. It is a qualification that is essential to successful auditing since the auditor's work involves conferences and interviews with all strata of personnel from the president of a company down to the office boy and factory worker.

A person with a pleasing personality, highly effective in human relations, and possessing a superior ability in communications, already has 70% of the necessary requirements for success, whether it be in auditing or some other professional activity. As important as technical knowledge may be, and it is important, very important, it constitutes only about 30% of the qualifications necessary for more than mediocre success.

The auditor with good technical training and experience plus a superior ability in communications and human relations is always in demand at an attractive salary.

**TAX NEWS** (Continued from page 5)  
tracts or the patents were the income-producing property, and held that the decisive question was whether the taxpayer had retained sufficient power and control over the assigned property to make it reasonable to regard him as the owner of all rights which he had prior to the assignments and the real recipient of the income. *Joseph Sunnen, U. S. Sup. Ct., April 5, 1948.*

The decision leaves undecided what the result would have been if the license agreement had been an exclusive one with a completely independent corporation. If the patents were held to be the income-producing property, the royalties would be taxed to the husband on the ground that there had been only an assignment of income.

\* \* \*

Heloise Brown has sent us a copy of a bulletin published by the Investment Bankers Association of America calling attention to the fact that the Bureau of Internal Revenue has recently modified one of the provisions of I.T. 3828, issued in December, 1946, which held that "a dealer in securities may treat as capital assets, as defined in Section 117(a)(1) of the Internal Revenue Code, securities acquired for investment purposes, provided it is established . . . (1)

that such securities are acquired and held for investment and are not part of those held for sale to customers, and (2) they are not of a type ordinarily sold to the dealer's customers."

It was the second clause that worked a hardship on firms which have been both dealers and investors in the same type of securities, and which had actual or potential gains in their investment portfolios.

On February 23, 1948, the Bureau issued I.T. 3891, modifying I.T. 3828 by now ruling that "where securities are acquired and held by a dealer in securities solely for investment purposes, such securities will be recognized as capital assets . . . even though such securities are of the same type or of a similar nature as those ordinarily sold to the dealer's customers."

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### CONGRATULATIONS TO DOROTHY OTTOWAY

The May issue of the *Mid Western Banker* contains a news item about the appointment of Dorothy Ottoway, C.P.A., a member of AWSCPA, as manager of the credit department of the Marshall & Ilsley Bank, Milwaukee. Miss Ottoway has been with the bank since her graduation from the University of Wisconsin in 1938.

# WHAT'S NEW IN READING

THEIA A. GEBBIE, Beverly Hills, California

**ANATOMY OF DEPRECIATION**, by Luther R. Nash, S.B., S.M. (Public Utilities Reports, Inc., Washington, D. C. 1947. 205 pages.)

This discussion of the still unsettled problems of the retirement of property is a dissection of depreciation accounting with logical relatings to accounting as a whole. References are made to court and commission decisions; and opinions other than those of the author are brought into the development of a suggestion. The methods of depreciating set forth concern the straight-line method, service lives, interest methods, and the reserve-size procedure; with the relative advantages of each brought out.

There is no advocacy of any sudden change of method as it is known any accepted procedure should have its foundation in experience. However, if records of past experience are incomplete, unreliable or questionable, it behooves the accountant to give attention to future planning which might lead to a more accurate depreciation accounting.

**FASHION FUNDAMENTALS**, by Bernice G. Chambers, M.A. (Prentice-Hall, Inc., New York 1948. \$6.35—481 pages.)

Fashion is the accepted manner of dressing as adopted by a group of people at a particular time. This book is an excellent text for the expert *and* an interpretation to the lay person of fashion's history, its social significance, opportunities in the fashion world, and how this field of endeavor really works.

There are down to earth examples to illustrate points to be emphasized which make lively reading. For instance, we all know that originals are eventually copied and can be obtained for a much lower price as they become more popular. But the rapidity of such a change is set forth by tracing the copy of a certain Sally Victor hat. The original custom-made hat cost \$35.00; in less than three weeks its duplicates were retailing for \$1.85. Naturally, that was a quickie; ordinarily, retailers can count on a much longer period.

We may not be concerned over the retailing problems charted in this book, but as women we cannot help but be interested in the information about what we wear and how the "experts" lead us around.

**THE TRADE OF NATIONS**, by Michael

A. Heilperin. (Alfred A. Knopf, New York, 1947. \$3.00—234 pages.)

His contention that economic problems are less difficult to understand than they are to settle is well illustrated in Mr. Heilperin's interpretations of foreign trade, capital investments, exchange operations, and cartels. International trade is an important part of world organization, and the United States is the nation to lead the world in better living through attack on international economic instability so as to increase living standards at home and abroad. National prosperity, involving high and steady employment, is an international problem.

The position of a free-enterprise country when confronted by a country having state-controlled foreign trade is one point aptly set forth. For this and other arising irregularities, an international trade organization is suggested to promote nondiscriminating trade.

**THE BISHOP'S MANTLE**, a novel by Agnes Sligh Turnbull. (The Macmillan Company, New York, 1948. 314 pages.)

The heartaches and triumphs of young Hilary Laurens are a combination of his zeal as the new minister of a large, fashionable city church and his love for the beautiful, gay Alexa who eventually becomes his wife. He is an honestly religious young man who found great strength in the example of his grandfather, the Bishop, who died at the time Hilary was assigned his church. Grandy left him much wisdom, but none that he needed more than the following: "Remember, there will be times. Just hang on even when you feel there's No One or Nothing there. Hang on, anyway."

Some of these times were when his wife was highly criticized for her participation in social affairs outside the church; when he tried to fight the owner of the worst tenement houses in the vicinity—the man who was the biggest donor of his parish; when he was an hour late to officiate at an important wedding; when "Tommy Tatler," the gossip columnist, was out to get him.

Then, just when his foundations seemed well laid with an easier course ahead, there came the war. Hilary struggles with his soul to find an answer as to his place in the conflict, and can find no solution but to join the forces to comfort the minds of the fighting men.

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